

**REPORT OF**

**TARGET MARKET CONDUCT EXAMINATION**

**OF**

**MANUFACTURERS LIFE INSURANCE COMPANY**  
**OF NORTH AMERICA**

**WILMINGTON, DELAWARE**

**AS OF**

**DECEMBER 31, 1996**

The Honorable Mike Kreidler  
Washington Insurance Commissioner  
Insurance Building  
PO Box 40255  
Olympia, Washington 98504-0255

Dear Commissioner Kreidler:

Pursuant to your instructions and in compliance with the statutory requirements of RCW 48.03.010, I have examined the corporate affairs and market conduct of:

Manufacturers Life Insurance Company of North America, NAIC #90425  
One Rodney Street, 10<sup>th</sup> Floor  
Wilmington, DE 19801

hereafter referred to as "the Company" or "MNA". The following report is respectfully submitted.

#### Scope of Examination

The examination was performed in compliance with the provisions of Washington insurance laws and regulations. The market conduct review followed the rules and procedures promulgated by the Office of the Insurance Commissioner (OIC) and the National Association of Insurance Commissioners (NAIC). The examination covered the period of January 1, 1992 through December 31, 1996. The scope of this examination was limited to Marketing and Sales Practices, Complaint Handling and Replacement Activity.

## TABLE OF CONTENTS

<b>Report Section</b>	<b>Page</b>
Salutation	2
Examination Report Certification	4
Foreword	5
Scope	5
Regulatory Standards	5
History of the Company	6
Marketing Plan	7
Advertising File/Illustration Diskettes	
Advertising	7
Illustrations	9
Agent Activity	
Agent Marketing & Training Materials	10
Audits	10
Agent Contracts	11
WA Agent Oversight & Agent Disciplinary Procedures	11
Agent Licensing & Appointments	12
Complaint Handling Procedures/Complaints	13
Replacement Practices	15
Monitoring Replacement Activity	17
Policy File Review	18
Regulatory Actions	20
Summary	21
Instructions	22
Recommendations	23
Appendices	24

## **EXAMINATION REPORT CERTIFICATION**

This examination was conducted in accordance with the Office of the Insurance Commissioner and National Association of Insurance Commissioners market conduct examination procedures. This examination was performed by Leslie A. Krier, Alan A. Hudina and Nancy L. Barnes who participated in the preparation of this report.

I certify that the foregoing is the report of the examination, that I have reviewed this report in conjunction with pertinent examination work papers, that this report meets the provisions for such reports prescribed by the Office of the Insurance Commissioner, and that this report is true and correct to the best of my knowledge and belief.

---

Leslie A. Krier, AIE, FLMI  
Chief Market Conduct Examiner  
Office of the Insurance Commissioner  
State of Washington

## **FOREWORD**

This target market conduct examination report is by exception and additional practices, procedures and files subject to review during the examination were omitted from the report if no improprieties were indicated. Throughout the report, where cited, RCW refers to the Revised Code of Washington and WAC refers to the Washington Administrative Code.

## **SCOPE**

### **SITUS**

This examination was a Level Two Target Market Conduct Examination conducted off site.

### **TIME FRAME**

The examination covered the company's operations for the period January 1, 1992 through December 31, 1996.

### **METHODOLOGY**

#### **Sampling Standards**

In general the sample for each test utilized in this examination falls within the following guidelines:

**92% Confidence Level  
+/- 5% Tolerance**

## **REGULATORY STANDARDS**

Samples are tested for compliance with standards established by the OIC. The tests applied to sampled data will result in an error ratio, which determines whether or not a standard is met. If the error ratio found in the sample is, generally, less than 5%, the standard will be considered as "met." The standard for agent licensing and appointment is not met if any violation is identified. This will also apply when all records are examined, in lieu of a sample.

For those standards that look for the existence of written procedures, or a process to be in place, the standard will be met based on the examiner's analysis of those procedures or processes. The analysis will include a determination of whether or not the company follows established procedures.

## **HISTORY OF THE COMPANY TERRITORY OF OPERATIONS MANAGEMENT**

The Manufacturers Life Insurance Company of North America (MNA) was admitted to the State of Washington on June 15, 1981. It was originally incorporated as Chubb/Colonial Life Insurance Company of America. In 1984, the Company was renamed North American Security Life Insurance Company and its present title was adopted in 1997. It is a wholly owned subsidiary of Manulife-Wood Logan Holding Company, Inc. which is ultimately owned by the Manufacturers Life Insurance Company which has an 85% ownership interest.

MNA is licensed for variable life and annuity products in Washington. Their taxable premium volume in 1996 in Washington was \$27,942,265. As of the examination date they had 457 agents appointed in Washington.

The company is licensed in the District of Columbia, Puerto Rico and all states except New Hampshire and New York.

A Board of Directors governs the company. The members are:

John David DesPrez III  
Theodore Francis Kilkuskie

John David Richardson

For operations in the State of Washington, the Company's administrative records are located in Boston, Massachusetts. Current policy record files are stored electronically through the use of optical scanning technology. However, older files are maintained as paper files and are stored off site with several document retention firms. MNA uses three (3) computer systems for policy administration. The Vantage 11.0 system is used for administration of all deferred annuities. The ABA System is used to administer immediate annuities and deferred annuities that have matured electing an annuity payout. The Venture Life product is administered on a separate system developed by outside software consultants.

### **Affiliates and Subsidiary Companies**

MNA is a wholly owned subsidiary of Manulife-Wood Logan Holding Company, Inc., which is ultimately owned by The Manufacturers Life Insurance Company (Manulife Financial, 85% ownership) and officers of Wood Logan Associates (15% ownership). MNA has 2 wholly owned subsidiaries, The Manufacturers Life Insurance Company of New York, which markets products in New York, and Manufacturers Securities Services, LLC, which is the principal underwriter of the variable contracts. Given the nature of the business of these two (2) subsidiaries, they will be excluded from this examination.

## **MARKETING PLAN**

The Company originally advised the examiners that they were unable to locate marketing plans for 1992 to 1994. With further investigation, the Company was able to provide documents entitled “Annuity Review and Outlook” for 1994 and an outline entitled “1995 Sales/Marketing Campaigns.”

Of note in the material provided was Section C in the Annuity Review Outlook for 1994. This section was titled “App-later processing.” This is a process that “allows brokers to write annuity business in a manner similar to the process used to purchase mutual funds.” It is also noted that it has “become the primary means of transacting business with two major clients.” Additionally, implementation of the practice was to commence with all other broker dealers who could support the process.

The Company was asked to provide complete details of the app-later processing and responded with a chart that outlined the “app-less” workflow. The Company was then asked to provide copies of the “app-less ticket”, contract, confirmation statement, confirmation/application and the welcome package referred to in the outline. A review of this information and the findings follow in the section of this examination titled Policy File Review.

The remainder of the material provided did not indicate references to vanishing premium policies, replacement programs or any non-compliant marketing practices.

**STANDARD 1 - The Company’s marketing plan did not contain references to vanishing premium policies, replacement programs, exchange programs, or other indicators of possible churning activity.**

**RESULT: The Company met this standard.**

## **ADVERTISING FILE/ILLUSTRATION DISKETTES**

### **Advertising**

The Company’s advertising file was reviewed pursuant to WAC 284-23-090. The advertising file contained copies of all advertising materials as statutorily defined. The syllabus provided by the Company listed 111 items. As the Company provided copies of each item contained on the syllabus with their initial response to the level two exam, each item was examined. This examination included both material designated for agent use only as well as that which was designated for public dissemination.

Of the 111 items, 12 that were designated for broker dealer use only were excluded from review, as the examiner judged them unrelated to the scope of this exam. Of the remaining 99 items, 40 did not disclose the full name and home office of the insurer in

violation of WAC 284-23-060(1). See Appendix A for a listing by form number of the material in violation.

No other issues were detected and the remaining material reviewed was in compliance.

The Company does not allow agents under any circumstances to publish anything concerning the policies or the business of the Company unless first submitted to the Company for approval, and authorized in writing. No agent created material was encountered in the advertising file. The Company utilizes a six (6) phase approval process for review of agent produced sales materials.

- Phase I – Preliminary Review by Product Support, Marketing Director and variable representative.
- Phase II – Company Wide Circulation – This involves the executive and several department heads from both the Company and Wood-Logan Associates.
- Phase III – Review and Incorporation of Comments – The sales and marketing writer incorporates the comments made during Phases I and II reviews and if requested returns the modified piece for re-review prior to Phase IV, NASD filing.
- Phase IV – NASD Filing – Once comments are received and incorporated, the piece is filed with NASD.
- Phase V – Client Firms Requiring Pre-Approval – Once the NASD comments have been received the piece is sent along with the NASD Comment Letter to the various firms requiring pre-approval.
- Phase VI – The Company then determines when and if the new piece needs to be filed with state insurance departments.

The Company was asked about any audits or supervision of agents completed during the exam period showing that they did a review to ensure that unauthorized materials had not been used. The Company responded that “MNA recognizes that the broker/dealers with whom it contracts, and the sub-agents appointed by those broker/dealers, operate in a highly regulated environment. Broker/dealers are subject to a complex scheme of SEC, NASD and state regulation that, among other things, requires them to...ensure suitability standards are met, undergo audits and adhere to licensing requirements.” Additionally, “MNA’s selling agreement in use during the exam period accordingly vests its broker/dealers with sole responsibility for the direct supervision of its sub-agents’ business activities.” The Company states that “MNA and its broker dealers communicated regularly about sub-agent activities.” However, the only specific documentation provided was regarding agent appointments and terminations.

Since the merger of MNA and North American Security Life Insurance Co. in 1996, MNA formed the U.S. Division’s Market Conduct and Compliance Management Department. This department monitors compliance with state and federal law at the Company, including compliance with state advertising regulations. Procedures for review of advertising materials have been in place and followed for some time. However, MNA



states that these procedures are not available in a comprehensive written format. Documentation of these procedures is still in the process of being completed.

### **Illustrations**

The Company was asked to provide a description and list of all policy illustration diskettes used during the exam period. The Company replied that “MNA does not use any illustration software for the issuance of our variable annuity contracts.” The Company stated, however, that their single premium variable life contract was sold with the aid of an illustration produced only by Wood Logan Associates, MNA’s wholesaling unit. The illustration produced by Wood Logan only projected fund values at hypothetical growth rates and did not illustrate past separate account performance. The Company states that the hypothetical growth rates were limited to a maximum of 12% per annum and that all asset-based contract charges were deducted from the hypothetical growth rate. Additionally, the illustration also projected fund values at current and guaranteed charges at a growth rate of 0%. The Company provided a copy of an illustration. The illustration adequately identified current and guaranteed maximum charges and provided adequate disclaimers relative to the investment risk.

**STANDARD 2 – All agent or vendor produced training materials were controlled by the Company and that the Company actively audited use of these materials.**

**RESULT: As the Company did not actively audit use of these materials until 1996, the Company did not meet this standard.**

**STANDARD 3 – The advertising file contained copies of all advertising material as statutorily defined, including copies of agent created advertising material, WAC 284-23-090 and WAC 284-23-020.**

**RESULT: The Company met this standard.**

**STANDARD 4 – Advertising materials complied with Washington Advertising Regulations, WAC 284-23-010 through WAC 284-23-080.**

<b>Number of advertisements</b>	<b>109</b>
<b>Number of advertisements reviewed</b>	<b>109 (100%)</b>
<b>Number in violation</b>	<b>40</b>
<b>Percent in violation</b>	<b>36.6% (outside 5% tolerance)</b>

**RESULT: The Company did not meet this standard.**

## **AGENT ACTIVITY**

### **Agent Marketing and Training Materials**

The Company advises that its product distribution is through independent broker/dealer channels and that agent training material would have its source at the broker/dealer level. The Company advises that “Wood Logan, MNA’s wholesaling unit, does provide training for all new and existing broker/dealers licensed to sell our products. The training is provided through Wood Logan Academy...” The Company provided a syllabus of training courses dated 5/18/95 with an effective date of 3/8/91. There were 20 courses listed. The Company provided an outline of the material for each course. There were mentions of tax-free exchanges and the “controlling documents of an annuity contract” therein defined as the prospectus, application and contract. In the 140 pages of the expanded outlines provided, the word replacement was never mentioned. Nothing related to replacement requirements was found in the material provided.

**STANDARD 5 - Agent communications did not encourage replacement of existing internal or external policies, special funding programs or other indicators of churning activity.**

**RESULT: The Company met this standard.**

### **Audits**

The Company advises that “MNA does not maintain any sales offices in the State of Washington,” and that their products are sold through independent broker/dealers. Therefore, there were no audits completed for agencies in the State of Washington during the examination period. The Company relies exclusively on its broker/dealers to maintain agent communication and supervision and “...to assure that all of their agents are appropriately trained and educated on the products that they sell and the jurisdiction that they sell in.” Under the Selling Agreement, the Company retains the ability to request information from its broker/dealers if it finds it “necessary to establish diligent supervision.” When asked, the Company was unable to locate any documents that indicated MNA had made any such request during the examination period.

The Company’s U.S. Division’s Market Conduct and Compliance Management Department, established in 1996, oversees the Compliance Management Program. Under the program, individual business unit compliance officers are accountable for agent activities and compliance issues. These compliance officers must report to management on a quarterly basis.

**STANDARD 6 – The Company conducted regular audits of agent activities through regular branch or agency office audits and visits.**

**RESULT: As the Company did not implement monitoring until 1996, the Company did not meet this standard.**

**STANDARD 7 – Training material for both new and existing agents in use during the examination period complied with Washington Statutes and Regulations, WAC 284-23-010 through WAC 284-23-130.**

<b>Total Number of Training Materials</b>	<b>20</b>
<b>Pieces reviewed</b>	<b>20 (100%)</b>
<b>Pieces not in compliance</b>	<b>0</b>
<b>Percent not in compliance</b>	<b>0% (within 5% tolerance limit)</b>

**RESULT: The Company met this standard.**

### **Agent Contracts**

MNA contracts with independent broker/dealers. MNA's wholesaling unit, Wood Logan, fosters the broker/dealer relationship. The broker/dealer firm, not MNA nor Wood Logan, determines the reporting structure of the broker/dealer. The Company utilizes one (1) Selling Agreement. This Selling Agreement stipulates that the selling broker/dealer "has full responsibility for the training and supervision of all persons...who are engaged directly or indirectly in the offer or sale of securities regulated contracts."

Neither the Selling Agreement nor the Selling Agreement's Commissions and Fees Supplement contained any language or compensation that would tend to encourage internal replacements. Commission adjustments are made for policy changes, conversions, and contract withdrawals that occur within specified time limits.

**STANDARD 8 – Agent contracts and commission schedules did not contain language that encouraged internal replacements.**

**RESULT: The Company met this standard.**

### **WASHINGTON AGENT OVERSIGHT AGENT DISCIPLINARY PROCEDURES**

The Company distributes its variable annuity products through third party broker/dealers. Oversight of the selling agents is the responsibility of the Selling Broker/Dealer and its registered representatives selling the variable product. This is a requirement of MNA's Selling Agreement. Additionally, the NASD mandates that suitability be addressed by the Broker and his firm through various requirements and responsibilities imposed upon them by the NASD. The Company requires each Broker/Dealer to sign an indemnification agreement which states that the firm must reimburse the Company for any and all losses, including attorney's fees, as a result of the Selling Broker/Dealer's or its representatives' failure to comply with the provisions of the selling agreement.

Therefore, if a Selling Broker/Dealer fails to comply with its NASD supervisory requirements and an unsuitable product is sold to a consumer, the Company can seek reimbursement from the Selling/Broker Dealer.

The Selling Agreement also states that “Selling broker/dealer shall fully comply with the requirements of the NASD...and all other federal or state laws. Selling broker/dealer shall establish such rules and procedures as may be necessary to cause diligent supervision of the securities activities of the sub-agents. Upon request by Manulife North America, broker/dealer shall furnish such records as may be necessary to establish diligent supervision.” The Company was asked if it had ever requested any records for review to determine if diligent supervision was being provided. The Company’s response, in part, was “Under the Selling Agreement, MNA retains the ability to request information from its broker-dealers if it finds it ‘necessary to establish diligent supervision’ by the broker-dealer. Although we have been unable to locate any written evidence that MNA made any such formal request under Section 4 of the agreement during the exam period, we have located documents which indicate that MNA and its broker-dealers communicated regularly about sub-agent activities.” The communication referenced was listings of terminated agents and confirmations of agents’ appointments.

The Company was asked if it had an ethics review board or similar entity and responded that “Such a board did not exist within MNA during the time period under review.” The Company also responded that an ethics review board has never been established.

**STANDARD 9 – The Company had and followed written procedures for disciplining agents and that actions are documented.**

**RESULT: The Company did not meet this standard.**

**AGENT LICENSING & APPOINTMENTS**

A review of 128 randomly selected policy data files was conducted. The agent listed on the application was checked against the State’s agent licensing system to identify any agent licensing or appointment irregularities. As numerous irregularities were found, the Company was asked to provide documentation that the agents were licensed and appointed when the applications in question were written. After reviewing the company’s documentation, the examiners found three (3) agents that were licensed but not appointed when soliciting business on behalf of the Company. This is a violation of RCW 48.17.010. Appendix B identifies the agent number, policy number, date of policy and appointment dates. Additionally, the Company provided policy database was checked for additional contracts written by these agents during the exam period. Where additional contracts were involved, those contract numbers are also included in the table.

**STANDARD 10 – Agents representing the Company had been licensed and appointed prior to soliciting applications on behalf of the Company, RCW 48.17.010.**

<b>Number of policies issued</b>	<b>3160</b>
<b>Number reviewed</b>	<b>137 (128 sample files plus 9 from company data)</b>
<b>Violations</b>	<b>11</b>
<b>Percentage</b>	<b>8% (0 tolerance)</b>

**RESULT: The Company did not meet this standard.**

*Subsequent Event: In 1998, MNA implemented the OMNI imaging system. This system brought more effective documentation capabilities as well as searching capabilities, which has assisted MNA to better record, document, and track agent licensing paperwork. The agent record is then added to the Distribution Support System database. When new business is received, the new business system, Vantage One, now validates against the Distribution Support System to ensure that the agent is appropriately licensed and appointed. If the agent is not actively appointed for the state in which the business was sold, or if the agent's license has expired, Vantage will not accept the new business until the licensing issues are resolved.*

The Company reported a total of 98 agent terminations during the examination period. This is consistent with OIC records. Of these 98 terminations, none were reported for cause.

**STANDARD 11 – All agents that had been terminated for cause by the Company had been reported terminated to the OIC.**

**RESULT: The Company met this standard.**

### **Complaint Handling Procedures/Complaints**

The Company provided a one-page narrative in response to the request for the Company's complaint procedures. The Company was asked if this one (1) page narrative constituted their entire complaint procedure. The Company responded that "The complaint handling procedures outlined...is (sic) in narrative form and not enumerated or formalized in any other form. The submitted narrative is what is used by the Manufacturers Life Insurance Company of North America when handling complaints."

The procedures indicate that all complaints received which involve a state insurance department, other types of regulatory agencies, an attorney representing the contract holder or any circumstances which may result in legal liability are immediately sent to the law department. The Company indicates that the majority of complaints are initially received by phone in the Company's Teleservice Department. The Teleservice Department sends the complainant to the law department, which requires complainants to submit their complaint in writing. All complaints are assigned a number by the law department for tracking purposes. Once the complaint is resolved, the number is transferred to the Complaint Register for permanent reference. One of the attorneys from

the Company's legal staff handles the majority of complaints. All others are handled by a paralegal that is supervised by an attorney.

The Company was asked if any reports were generated based upon the complaints. The Company responded that "a confidential, written report of complaints in Manulife's U.S. Operations, including MNA, is prepared and presented quarterly to the U.S. Operations senior management team."

**STANDARD 12 – The Company had and followed written complaint handling procedures.**

**RESULT: The Company met this standard.**

In summary, the Company follows their written complaint handling procedures. The Company's procedures do not specifically address tracking trends; however, given the quarterly report to senior management, the number of complaints received and the involvement of the law department in reviewing all complaints, the procedures in place indicate the Company would be aware of trends in the complaints and would be able to act upon them accordingly.

**STANDARD 13 – The Company monitored complaint records for trends, and had a formal procedure for reporting trends to management.**

**RESULT: The Company met this standard.**

During the exam period, MNA received a total of four (4) complaints. All four (4) of these complaint files were requested and reviewed. One involved a question as to the maturity date of the contract, two (2) others were administrative in nature and the fourth involved a policyholder that appeared confused as to what he had purchased. The complaints were resolved in 15 working days or less. In all cases the Company's procedures as outlined above appear to have been followed.

**STANDARD 14 – The Company responded to OIC complaints within 15 business days (WAC 284-30-650) and showed good faith in resolving complaints within 15 business days.**

<b>Total number of complaints</b>	<b>4</b>
<b>Policy files reviewed</b>	<b>4</b>
<b>Number outside of 15 day turnaround</b>	<b>0</b>
<b>Percent outside of 15 day turnaround</b>	<b>0 (within 5% tolerance limit)</b>

**RESULT: The Company met this standard.**

## **REPLACEMENT PRACTICES**

The Company responded with a one (1) page narrative to the request that they provide their replacement procedures during the exam period. The Company was asked if this narrative did in fact encompass and represent their replacement procedures. The Company responded that “The replacement procedures provided...is (sic) a documentation of the replacement procedures for the period of the examination. These procedures are not documented in any other form.” In addition to the narrative, a copy of WAC 284-23-410, 430, 440, 450 and 455 as well as copies of the replacement notice were attached.

The Company states that “as a practice, we do not allow accounts to be internally exchanged.” However, the Company does allow like contracts for the same annuitant and owner to be combined. When asked for specifics on how surrender charges are combined on contracts of differing surrender charge periods, the Company responded that the client receives credit for “time served” with the Company. No new or additional surrender charges are added to the contract. In most instances, the older of the two contracts remains active and the funds from the newer contract are moved into the older contract. The Company emphasized that these contract combinations do not benefit the Company but do provide some benefit to the contract owner. The client is able to maintain one contract without being assessed additional surrender charges. In addition, there is now only one contract with administrative fees rather than two. The agent/broker receives no compensation for this type of transaction, and contracts are only combined at the client’s request. The Company does allow contractual changes such as conversions, if allowed by contractual provision.

If replacement forms are with an application, a Notice of Replacement of Existing Insurance is sent to the existing company. For replacement applications without replacement forms, the Company states “No correspondence or exchange request is mailed to the surrendering carrier until all contract paperwork is in good order.” This is in violation of WAC 284-23-455(2)(b) wherein it states that “written communication [to the existing company] shall be made within three working days of the date the application is received in the replacing insurer’s home or regional office...”

It should be noted that the Company’s replacement procedures do not require an amendment be obtained if either the applicant’s replacement question or agent’s replacement question on the application is left blank. This is a violation of WAC 284-23-450(2). This regulation states that a company must “Require with or as part of each completed application for life insurance or annuity a statement signed by the applicant as to whether such proposed insurance or annuity will replace existing life insurance or annuity.”

If the replacement question on the agents report is left blank, it is a violation of WAC 284-23-455(1) which states “Require with or as part of each completed application for

life insurance or annuity, a statement signed by the agent or broker as to whether he or she knows replacement is or may be involved in the transaction.”

A review of 128 randomly selected policy files from the Company provided database of policies issued during the exam period was conducted. Replacement was involved in 32 of the 128 files. The examiners believed the sample was an adequate number of files to provide an accurate representation to test replacement compliance. In the 32 replacement files, the following violations were noted:

- There were 15 contract files that did not contain a statement signed by the applicant as to whether or not replacement was involved.
- There were 20 contract files that did not contain a statement signed by the agent as to whether or not replacement was involved.
- In five (5) instances, there was not a copy of the notification letter to the existing company concerning possible replacement of their policy.
- In three (3) cases, the notification letter was sent more than 3 days after the application had been received by MNA.
- One (1) contract file did not have a signed replacement form.

See Appendix C for details of the above findings.

Additionally, files that indicated replacement was involved were checked against the Company’s replacement log and all indicated replacement files appeared on the Company’s log. However, the Company’s replacement log was not cross-referenced to reflect the existing insurer to be replaced. This is a violation of WAC 284-23-455(3) wherein it states, “The replacing insurer shall maintain ... and a replacement register, cross indexed by replacing agent and existing insurer to be replaced.”

A review of the Company provided data relative to loans, withdrawals and surrenders was unremarkable for any replacement issues.

**STANDARD 15 – The Company’s replacement procedures were in writing and were consistent with the Washington Replacement Regulations.**

Code	Total Population	Sample	# of Violations	Percentage in Violation
WAC 284-23-450(2)	128	32	15	46.9%
WAC 284-23-455(1)	128	32	20	62.5%
WAC 284-23-455(2)(a)(ii)	128	32	1	3.1%
WAC 284-23-455(2)(b) letter	128	32	5	15.6%
WAC 284-23-455(2)(b) 3 days	128	32	3	9.4%

**RESULT: The Company did not meet this standard.**



*Subsequent Event: MNA has taken several steps aimed at ensuring that it is in compliance with Washington State replacement regulations. A replacement matrix that indicates which states require replacement forms was enhanced in 1998 and has been updated annually. In addition, a replacement workflow and a replacement database are currently being created for completion in 2001. These measures, when implemented, will assure that replacements are being processed in compliance with state regulation.*

## **MONITORING REPLACEMENT ACTIVITY**

NOTE: There is no legal limit as to the number of replacements an agent may write. However, replacements should be monitored by the companies to guard against excessive replacement, or churning. The threshold of “greater than one (1) per month” is used in this section of the examination solely for the purpose of testing company oversight procedures.

There were 3,160 contracts issued during the examination. The Company’s replacement log indicates 1,123 entries. This is approximately 35.5% of the Company’s business with a source of replacement.

Information was extracted from data provided by the Company which indicated 21 agents, each of whom had written more than 10 contracts, had replacement as the source of 50% or more of their business. The Company was asked if they monitored the replacement log for high levels of replacement activity by agent. Their response was “...that it (MNA) had no procedures in place that established a ‘ceiling’ on replacements, nor were there procedures in place that established a threshold percentage that would trigger an agent inquiry.” These 21 agents wrote 596 contracts of which 393 were replacements (66%).

**STANDARD 16 – Number of replacements for any one agent in any calendar year should not be significant (<1 per month, combined internal and external replacements).**

**RESULT: The Company did not meet this standard.**

**STANDARD 17 – The Company had identified patterns of replacements by individual agents such as moving policies in and out of the Company at regular intervals, replacements of large blocks of business, moving funds from one policy to another.**

**RESULT: The Company did not meet this standard.**

*Subsequent Event: The creation of a replacement database, due to be completed in 2001, will automate the tracking of both internal and external replacement activity. This system is being designed to track the name of the agent, the broker/dealer, the client’s name, contract number, and the name of the existing insurer.*

## **POLICY FILE REVIEW**

The number of Washington policies in force as of 12/31/96 was 24 variable life policies and 3,680 variable annuities. The total number of policies issued in Washington from 1/1/92 to 12/31/96 was 3,159. From the 3,159 issued policies, 128 policy files were selected at random and requested from the Company for review by the examiners. The policy files were reviewed with emphasis on the following areas:

- Did both the applicant/owner and the agent properly sign the application?
- Was the agent appointed by the Company and licensed by the state when the application was signed?
- Was replacement of an existing contract involved and if so were the proper replacement forms completed? If an external replacement, was proper notification provided to the existing company?
- Were existing policy values used to pay the premium on the new policy?

The review of policy records did not indicate a pattern of old policies being used to fund new policies.

The Marketing Plan section of this examination references App-less processing. As indicated, the review of this application processing method was deferred until this section of the examination. There are two (2) forms used in the app-less process. The first is an App-less Ticket (AT) which is a policy specification sheet describing the plan applied for, the investment allocation, beneficiary, owner and agent information. The second is a Confirmation of Application (CA) form that combines a welcome letter with an AT form that contains space for the owner's signature and the date signed.

The Company's app-less workflow indicates that once the agent and owner complete the AT, it is then sent to MNA via mail or fax. The information from the AT is then entered into MNA's System. Policy pages are generated which include two (2) copies of the CA. One (1) is included in the policy in place of an application form. The other is sent with the policy to be signed by the agent and owner, then returned to the Company for file documentation. Until the signed CA is returned, financial transactions are not to be processed against that policy with the exception of premium payments. As noted in the following paragraphs, the Company does not follow these procedures.

The Appless Workflow procedure also indicates that if the form is not returned, the Company will:

- send a follow up letter to the agent after 30 days;
- re-send the contract to the client by certified mail after 60 days;
- notify the broker/dealer of all unsettled accounts after 120 days.

Additionally, the Company's procedures state that the "account (is) restricted from redemption until signed Confirmation/Application is received." Our review indicated that the Company allowed transactions against a policy without a signed CA on file.

The Company advises that 30 contracts were issued on an app-less basis in Washington during the exam period. Of those 30, 29 policy files were reviewed. The Company could not locate one (1) policy file. The findings of this review are as follows:

- There were 10 files where the CA had never been returned to the Company.
- There were two (2) files where the CA was more than four (4) months after the date the policy was mailed to the owner.
- There was one (1) file where the CA was signed and returned, but not dated.
- There were (2) files where changes were made to the contract without a signed CA on file. One was a name change; the other was a change to investment options.
- There were two (2) files where full surrenders were processed. One file required that a signature guarantee be obtained, the other did not.

See Appendix D for contract detail.

The above app-less processing findings indicate that approximately 33% of all business processed on an app-less basis were not in compliance with the Company's own stated procedures for processing this business.

The remaining specific findings of this review are incorporated into the sections of this report entitled Replacement Practices and Agency Licensing/Appointments.

*Subsequent Event: The Company updated its optical workflow distribution system in April 1998. The new system, OMNI, greatly improves the Company's ability to identify and track the date documents are received at their offices. The system scans all incoming documents, leaving a permanent time and date stamp stored in the OMNI system. This time and date stamp cannot be altered.*

## **REGULATORY ACTIONS**

A review of the disciplinary actions taken by other states within the last 5 years indicates 3 actions. These actions are summarized below.

- 1) State of Wisconsin, 1999 – the Company paid a civil forfeiture to the Office of the Commissioner of Insurance, for failure to respond to a licensing related inquiry in a timely manner.
- 2) State of Oregon, 1997 – the Company agreed to execute a consent order and pay a civil penalty of \$2000.00 for allowing an agent to write a policy on a resident of Oregon without the agent being licensed in Oregon. It should be noted that the agent indicated that the sale occurred in Missouri and while the Company questions the constitutionality of this particular provision, the Company nonetheless chose to settle the matter.
- 3) State of Delaware, 1997 – the Company paid the Delaware Insurance Department a fine of \$500.00 for failure to file a Form D Filing. The Company had interpreted section 5005 of the Delaware Insurance Code as including separate account assets in the definition of admitted assets. The Delaware Insurance Department stated that a Form D Filing was required since separate account assets are not considered admitted assets for holding company filing purposes.

## SUMMARY

Since the examination period of 1992 – 1996 was a number of years ago, MNA did encounter some difficulty in producing documentation in certain instances. In addition, producing requested information was made more difficult by two factors. First, on January 1, 1996, in a merger with North American Life Assurance Company, Manulife acquired North American Security Life Insurance Company, and subsequently renamed it The Manufacturers Life Insurance Company of North America (MNA). Secondly, MNA underwent two major system conversions since 1992, impacting many of MNA's operations, including agent licensing and appointments and replacements.

It is apparent that MNA relies heavily upon the oversight provided by the Company's broker/dealers, who are licensed and subject to the rules of the NASD, and by agreement, indemnify the Company against losses. However, the Company has realized the importance of their need to maintain control, and in 1996, created a department responsible for monitoring and reporting compliance issues.

This examination has pointed out inadequacies in the Company's processes and procedures. Adherence by the Company to its own stated procedures, most notably in the area of replacement processing and regarding app-less processing, is inconsistent. However, the Company is demonstrating their desire to meet compliance standards by implementing new systems to ensure operational oversight.

## MNA INSTRUCTIONS

- 1) The Company is in violation of WAC 284-23-060(1) and is instructed to make certain that its full name and home office are clearly identified on all advertisements. (Pages 7, 8 and 9).
- 2) The Company is in violation of WAC 284-23-455(2)(b) and is instructed to change its procedures such that “written communication [to the existing company] shall be made within three working days of the date the application is received in the replacing insurer’s home or regional office...” (Page 15).
- 3) The Company is in violation of WAC 284-23-450(2) and is instructed to “Require with or as part of each application for life insurance or annuity a statement signed by the applicant as to whether such proposed insurance or annuity will replace existing life insurance or annuity.” (Page 15).
- 4) The Company is in violation of WAC 284-23-455(1) and is instructed to “Require with or as part of each completed application for life insurance or annuity, a statement signed by the agent or broker as to whether he or she knows replacement is or may be involved in the transaction.” (Page 15).
- 5) The Company is in violation of WAC 284-23-455(2)(b) and is instructed to “Send to each existing insurer a written communication advising of the replacement or proposed replacement...” (Page 16).
- 6) The Company is in violation of WAC 284-23-455(3) and is instructed to change its replacement register to include the name of the existing insurer to be replaced. (Page 16).
- 7) The Company is in violation of WAC 284-23-455(2)(a)(ii) and is instructed to “Require...a copy of the replacement notice provided the applicant pursuant to WAC 284-23-440(2)(a). (Page 16).

## **MNA RECOMMENDATIONS**

- 1) It is recommended that the Company establish formal written procedures for disciplining agents and that written documentation be maintained of any actions taken. (Page 12).

<b>APPENDIX A</b>	
<b>MNA – Listing of advertisements in violation of WAC 284-23-060 (1). "The full name and home office of the insurer shall be clearly identified..."</b>	
<b>FORM NUMBER</b>	<b>FORM NUMBER</b>
VEN 3 02923M:6202	1195:954
ven1092 20m:608	0795 50m:206
0292 50m:601	0795:601
1192 15m:10	0495:V189T
VEN 1092 375m:705	0195 35m:206
PRA 30192 5m:255C	VEN 0195:3804
VEN 0293:949	VEN 0495:3803
VV 0393 50m: 9003	1095:4004
1093 6M:258	ENH VEN 0495:3003
VEN 1093 11m:810	3953009
1193 50m:272	VV1195:9004
0393 20m:601	Enh VEN 0196:208
VV 0893:9014	0796:71306(207)
0294 50m:615	0696:70806 (616)
0894:958	0696:(15m)81482
0194 25M 954	0196 55M:206
0194:956	VEN 0996:70505
VV0394:9013	Enh VEN 0996-70501
VV1194 9002	VV 0396:5003
Enh Ven 0495:208	VV 0996:60503



## APPENDIX B

Contracts Written by Unappointed Agents			
Agent Number	Policy Number	Policy Date	Appointment Dates
2789451027	713257	2/8/93	Appointment expired 6/15/91
	713974	2/17/93	Appointment expired 6/15/91
	713975	2/17/93	Appointment expired 6/15/91
	713976	2/17/93	Appointment expired 6/15/91
	713977	2/17/93	Appointment expired 6/15/91
	713978	2/17/93	Appointment expired 6/15/91
	713979	2/17/93	Appointment expired 6/15/91
	720112	4/27/93	Appointment expired 6/15/91
	792972	12/8/93	Appointment expired 6/15/91
63649037	231807	3/16/92	Appointed 3/19/92
	230907	3/18/92	Appointed 3/19/92
WA-04268	835053	6/6/95	Appointed 3/3/88 to 6/15/92 and
			7/6/95 to 6/15/2000

## APPENDIX C

Replacement Violations – Excluding App-less Processing		
Code/Description	# of Violations	Policy Numbers
WAC 284-23-450(2) - Replacement, Submit statement signed by applicant.	15	126711, 127441, 127444, 713257, 793320, 814133, 825489, 125305, 741459, 813308, 300435, 302215, 835053, 744407, 851615
WAC 284-23-455(1) - Replacement, Submit statement signed by agent.	20	126690, 127441, 702261, 711585, 713257, 715941, 715943, 715959, 715965, 731791, 825489, 125305, 234458, 700437, 725292, 741119, 810395, 813516, 818145, 302215
WAC 284-23-455(2)(a)(ii)- Replacement, Signed replacement notice.	1	835053
WAC 284-23-455(2)(b) – Replacement, Send notification letter to existing insurer. Copy of letter not in file.	5	400701, 400758, 400802, 400853, 715647
WAC 284-23-455(2)(b) – Replacement, Send notification letter to existing insurer within 3 working days of the date the application is received in home or regional office.	3	709182, 850312, 850844

## APPENDIX D

App-less Processing Inconsistent with Company's Stated Procedures		
Inconsistency	#	Policy Number/Specifics/Dates
<b>Confirmation of Application (CA) Never signed - no follow up Noted in the file by the Company to Obtain the owner's signature.</b>	10	744029, 743991, 744482
		744419, 744206, 744205
		744199, 744824, 743757
		744285
<b>Date on Confirmation of Application Greater than 4 months from the time The appless ticket was written</b>	2	744833 – contract date 8/22/96, CA date 12/1/98
		870511 – contract date 10/29/96, CA date 4/14/97
<b>Confirmation of Application signed, Not dated</b>	1	870280
<b>Contractual change to contract Without owners signature on CA</b>	2	744029 – changed investment options 9/23/97
		743991 – name change request from agents assist.
		With copy of marriage cert. but no owner's sign
<b>Full surrender of contract without Owner's signature on CA</b>	2	744285 – owners sign. on request only, no signature guarantee
		743757 – request had a signature guarantee